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Supreme Court of the United States

OCTOBER TERM, 1976

No. 76-1013

TEXAS EASTERN TRANSMISSION CORPORATION,
a Delaware Corporation authorized to do business in New Jersey,
Appellant,

vs.

WILLIAM KINGSLEY, Director of the Division of Taxation,
Department of the Treasury, State of New Jersey,
Appellee.

ON APPEAL FROM THE SUPREME COURT OF NEW JERSEY

JURISDICTIONAL STATEMENT AND APPENDIX

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SUPREME COURT OF THE UNITED STATES

October Term, 1976
No.

TEXAS EASTERN TRANSMISSION CORPORATION, a Delaware Corporation authorized to do business in New Jersey,

Appellant,

vs.

WILLIAM KINGSLEY, Director of the Division of Taxation, Department of the Treasury, State of New Jersey,

Appellee.

ON APPEAL FROM THE SUPREME COURT OF NEW JERSEY

JURISDICTIONAL STATEMENT

The jurisdiction of this Court is invoked pursuant to 28 U.S.C. §1257(2), this being an appeal which draws into question of the validity of the New Jersey Corporation Business Tax Act, N.J. STAT. ANN. §54:10A-1, *et seq.*, as applied to this taxpayer on the grounds that it is repugnant to the Constitution of the United States. The constitutional issues were raised by brief in the various state proceedings below. Appellant's appeal to the New Jersey Supreme Court was dismissed on October 25, 1976. A Notice of Appeal was filed with the New Jersey Supreme Court on January 5, 1977.

OPINIONS BELOW

The Order of the Supreme Court of New Jersey dismissing Appellant's appeal which is as yet unreported, is set forth in the Appendix, *infra* (p. 47a). The *per curiam* Opinion of the Appellate Division of the Superior Court of New Jersey affirming on the Opinion below, also unreported, is set forth, *infra* (p. 45a). The Opinion of the Division of Tax Appeals is unreported but is set forth, *infra* (pp. 14a-41a).

QUESTIONS PRESENTED

1. Whether the use of the three-factor (Massachusetts) formula addressed by this Court in *Northwestern States Portland Cement Co. v. Minnesota*, 358 U.S. 450 (1959), which as applied unfairly apportions a particular corporation's net income and net worth violates the Commerce Clause of Article I, Section 8 and the Due Process Clause of the Fourteenth Amendment of the United States Constitution.

2. Whether on the uncontested facts of this case, an apportionment to New Jersey of a percentage of the Appellant's net income and net worth by inclusion of values found to have no real relationship to that state, constitutes such an unfair apportionment.

3. Whether the cumulative impact of successive taxation, on or measured by gross receipts in the transfer of natural gas in interstate commerce, imposes a multiple burden "on commerce."

STATEMENT OF THE CASE

The fundamental issue in this case involves New Jersey's taxation, by purported use of a formula tax, of transfers of gas in continuous flow in interstate commerce predestined by certificates of public convenience and necessity issued by the Federal Power Commission for use elsewhere.

The Appellant Texas Eastern Transmission Corporation is an interstate natural gas company that purchases natural gas principally in Texas and Louisiana producing areas for transmission at high speeds and under high pressure through a multistate network of pipelines to markets in the Midwest and Northeast United States. All such shipments are made pursuant to certificates of public convenience and necessity issued by the Federal Power Commission which has exclusive jurisdiction to control deliveries under the terms of the Natural Gas Act. 15 U.S.C. §717 *et seq*. The FPC also regulates Texas Eastern's rates, charges and earnings.

In 1967, the tax year at issue (the treatment of succeeding years being dependent upon the outcome of this appeal), Texas Eastern's New Jersey business consisted chiefly of delivering natural gas to three New Jersey public utilities for redistribution to home and industrial users within that state. Only two and a-half percent (2.5610%) of the company's pipeline was located in New Jersey. It had no sales or business office whatever in New Jersey, although it did have one small maintenance facility. The company employed twenty-nine (29) people in New Jersey, representing less than one percent (0.9789%) of its payroll. It did own substantial property in New Jersey, mostly underground pipelines and metering stations, but even this constituted only four percent (4.0412%) of the company total. Less than ten percent (9.9602%) of Texas

Eastern's total gross receipts were derived from sales to New Jersey utilities.

Unlike New Jersey utilities, Texas Eastern is subject both to an *ad valorem* tax and a corporate franchise tax. In 1967, Texas Eastern paid $701,603 in *ad valorem* taxes, $1,059 in miscellaneous taxes. In addition, even if Texas Eastern were to be completely successful on this appeal, it will still have paid $93,659 as its corporate franchise tax.

The New Jersey Business Corporation Tax is a franchise tax levied on a corporation's apportioned net worth and net income. The apportionment is based upon the corporation's relative business activity in the state. A percentage allocation factor is determined by a composite formula of relative property, payroll and gross receipts in the state.

Application of New Jersey's formula by use of the above factors, including all New Jersey destination receipts, would result in a finding that less than 5% of Texas Eastern's 1967 activity was in New Jersey. Appellant regards that percentage high, but not a constitutionally unreasonable result.

However, in addition to use of the New Jersey destination receipts in the formula, the state's Director of the Division of Taxation also included receipts for natural gas transferred in New Jersey by Appellant to Algonquin Gas Transmission Company, another interstate natural gas company, for uninterrupted, continuous flow out of New Jersey to meet FPC directed deliveries in New York and New England. These bulk transfers, which were made from Texas Eastern's pipelines to Algonquin's without slowdown in transmission speed, and which could not lawfully be diverted for use in New Jersey, accounted for almost 13% of all of Texas Eastern receipts everywhere for the tax year in question.

Use of the Algonquin receipts as part of the business allocation factor in the New Jersey formula resulted in a virtual doubling of Texas Eastern's estimated "presence" in New Jersey with a concomitant doubling of its tax liability.[1]

Texas Eastern sought immediate judicial relief from the Director's determination. After various delays caused by court congestion, this matter was submitted to the New Jersey Division of Tax Appeals on a Stipulation of Facts (pp. 1a-13a) in 1972. In June of 1975, that court denied all relief in an opinion (pp. 14a-41a) which was filed only after the Appellant had brought a formal motion to compel a decision.[2] Thereafter, the Appellant applied to the Appellate Division of New Jersey's Superior Court for review.[3] The Appellate Division rendered a *per curiam* opinion of affirmance based upon the trial court opinion. (p. 45a) Thereafter, Appellant filed both a Petition for Certfiication seeking review by the New Jersey Supreme Court of the state law issues, and a Notice of Appeal seeking review as a matter of right on the constitutional questions. The Petition was denied (p. 46a) and the Appeal dismissed. (p. 47a) A Notice of Appeal to this Court has been filed. (p. 48a)

The determination of the trial court (left undisturbed by the Appellate Division and the New Jersey Supreme Court) to include the Algonquin receipts, as part of the New Jersey receipts portion of the business allocation fac-

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1. Some $80,000 was added to the company's franchise tax liability for 1967 alone. Additional tax liability by reason of continuous inclusion of Algonquin transfers in succeeding years now exceeds $1,000,000.

2. The trial court's opinion (for which the Appellant waited three years) in its statement of the law is no more than a free dictation from the state's brief.

3. While this matter was pending before the Appellate Division of the Superior Court, Appellant sought direct review from the New Jersey Supreme Court in view of the inevitability of appeal. However, its motion for direct certification was denied (p. 44a).

tor, is made all the more incredible by the court's express finding that New Jersey had little or nothing to do with the underlying gas transfers:

> New Jersey is only remotely and incidentally connected with the interstate transaction. The natural gas flowed from wells in Texas and Louisiana into Texas Eastern's interstate pipeline system; transported through southern and midwestern States. It passed uninterrupted and at high pressure into Algonquin's interstate pipeline system and continued its interstate journey at high pressure in Algonquin's pipelines to its ultimate destinations out of New Jersey. The gas was thus carried from States outside New Jersey, through New Jersey in Texas Eastern's and Algonquin's interstate systems to distributors outside New Jersey in unbroken movement in the stream of interstate commerce.
>
> In reality, New Jersey is just one of the many States through which the gas passed in the flow of commerce and, by geographical circumstance, merely happened to be the place where the gas moved without pause or interruption from one interstate pipeline to another. The transfer was an integral, inseparable part of the interstate process. Without it, there could be no interstate commerce. [p. 26a-27a, *infra*]

Thus, by an unreasonable mechanical application of an apportionment formula New Jersey exacted a tax based in most significant proportion upon a transaction in which its interest has been found to be remote and incidental.

THE FEDERAL QUESTIONS ARE SUBSTANTIAL

I.

Whether the use of the three-factor (Massachusetts) formula addressed by this Court in *Northwestern States Portland Cement Co. v. Minnesota*, 358 U.S. 450 (1959), which as applied unfairly apportions a particular corporations's net income and net worth violates the Commerce Clause of Article I, Section 8 and the Due Process Clause of the Fourteenth Amendment of the United States Constitution.

Ever since this Court in *Maine v. Grand Trunk Ry. Co.*, 142 U.S. 217 (1891) first sustained the levy of a tax based upon a formula apportionment of the property of an interstate railroad, the Court has been willing to face the question of whether a formula fair on its face is in its application unfair to the railroad concerned.

Twice this Court struck down railroad mileage apportionment formulas where their effect was to subject to taxation values without the state. *Wallace v. Hines*, 253 U.S. 66 (1920); *Norfolk & Western Ry. Co. v. Missouri State Tax Comm'n*, 390 U.S. 317 (1968). In the latter case, Justice Goldberg, speaking for the Court stated:

> A State will not be permitted, under the shelter of an imprecise allocation formula or by ignoring the peculiarities of a given enterprise, to project the taxing power of the State "plainly beyond its borders." [Citations omitted.] Any formula used must bear a rational relationship both on its face and in its application to the property values connected with the taxing State. [at 325]

In *Wallace v. Hines* Justice Holmes, after discussing the justification for permitting apportionment, noted:

> The purpose is not to expose the heel of the system to a mortal dart—not, in other words, to open to taxation what is not within the state. [at 69]

In the related, but economically more significant, area of apportionment of net income and net worth of multistate corporations, little recent guidance has been provided by this Court to protect against the understandable tendency of state taxing authorities to maximize taxes.

Dicta in early net income apportionment cases indicated a concern by this Court that state formulas fair on their face might in fact produce an unreasonable result. *Underwood Typewriter Co. v. Chamberlain*, 254 U.S. 113, 121 (1920); *Bass, Ratcliff & Gretton, Ltd., v. State Tax Comm'n*, 266 U.S. 271, 283 (1924). And, of course, in *Hans Rees' Sons v. North Carolina*, 283 U.S. 123 (1931), this Court so held as to an obviously over-reaching tax imposed by a single factor formula.

The great change in Commerce Clause interpretation which has occurred since 1931, and the development of sophisticated formulas coupled with the silence of this Court for four and one-half decades, lends credence to a belief by taxing authorities that unreasonable results are no longer subject to this Court's supervening control of interstate commerce. The virtual absence of state court opinions following *Hans Rees' Sons* is telling.[4]

There is no uniformly applied system of state taxation of multistate corporations. Current Commerce Clause interpretation permits the imposition of state taxes based

4. See *F.W. Woolworth Co. v. Director of the Division of Taxation*, 45 N.J. 466, 213 A.2d 1 (1965) where the New Jersey Supreme Court *did* find a reversible misapportionment of the net income and net worth of the taxpayer to New Jersey, but the court summarily dismissed the contention that the Commerce Clause was violated.

upon apportionment systems which are in themselves reasonable even if the combined effect of the use of such systems produces overlapping taxation.[5] This approach has been approved by many commentators. See, *e.g.*, Hellerstein, *State Taxation under the Commerce Clause: An Historical Prospective*, 29 VAND. L. REV. 335, 345 (1976). But such an approach makes imperative a clear ruling by this Court that it will not tolerate unreasonable results produced by the blind application of formulas. *See Norfolk & Western, supra*, 390 U.S. at 325. Justice Frankfurter accurately predicted the necessity for review by this Court of the constitutionality of the results of the application of the formula here in question in his dissent in *Northwestern States, supra*, 358 U.S. at 474-75. For the Court to fail to provide for such review would, in the words of Justice Holmes, expose the system to a "mortal dart." As one writer has stated:

> The court's failure to provide effective limitations has convinced many state officials that they have complete control of the apportionment of income of any taxpayer. . . .[6]

Other approaches for insuring fairness to the taxpayer seem to have failed. The Multi-State Compact has not succeeded.[7] The decade of stalemate in Congress after the

5. *Compare Chase Brass & Copper Co. v. Franchise Tax Bd.*, 400 U.S. 961, *dismissing mem.*, 10 Cal. App. 3d 496, 95 Cal. Rptr. 805 (1970), *with Kennecott Copper Corp. v. State Tax Comm'n*, 409 U.S. 973 (1972), *dismissing mem.*, 27 Utah 2d 119, 493 P.2d 632 (1972).

6. W. Beaman, PAYING TAXES TO OTHER STATES (1963), at 3-18.

7. Congress has not ratified the compact; less than half of the states have joined; Illinois and Florida have recently withdrawn as compact members, P-H STATE & LOCAL TAXES, ALL STATE'S UNIT, ¶5,150; California has joined the compact on condition that the interstate arbitration provision, which has been suspended, remain suspended, R. Krol, 43 J. TAX 364, 365 (1975); and the interstate audit procedure (which has not been universally adopted even by party states) is under serious constitutional attack, *United States Steel Corp. v. Multi-State Tax Commission*, Civil No. 72-3438 (three judge court, S.D.N.Y., argued February 3, 1976).

issuance of the WILLIS REPORT[8] suggests that there will be no Congressional action, despite the repeated entreaties of this Court. See *Northwestern States, supra,* 358 U.S. at 476-477, Justice Frankfurter dissenting. In the meantime, the natural temptation of states and state tax administrators to "export taxes" by imposing them on non-voting out-of-state taxpayers continues. See E. Corgin, *Interstates Corporate Income Taxation—Recent Revolutions and Modern Response,* 29 VAND. L. REV. 423 (1976).

Thus the time is ripe and the circumstances appropriate for this Court to make an affirmative determination in this case that the results of the application of apportionment formulas are subject to the same scrutiny under the Commerce Clause of the United States Constitution as the formulas themselves.

II.

Whether on the uncontested facts of this case, an apportionment to New Jersey of a percentage of the Appellant's net income and net worth by inclusion of values found to have no real relationship to that state, constitutes such an unfair apportionment.

This Court in *General Motors Corp. v. District of Columbia,* 380 U.S. 553 (1965) stated that net income apportionment formulas must be related to "corporate activities within the State" and suggested that apportionments are justifiable as practical approximations of a corporation's source of income or the social costs it locally generates. Justice Brennan, dissenting in *General Motors Corp. v. Washington,* 377 U.S. 436 (1964), had earlier made the point:

8. REPORT OF THE SPECIAL SUBCOMMITTEE ON STATE TAXATION OF INTERSTATE COMMERCE OF THE COMMITTEE ON THE JUDICIARY, HOUSE OF REPRESENTATIVES, June 15, 1964.

> [I]t is the commercial activity within the State, and not sales volume, which determines the State's power to tax, and by which the tax must be apportioned. [at 450-451][9]

Thus, apportionment formulas are permissible only if they reasonably measure relative commercial activity within a state. Clearly then, the specific application of a given formula should be judged by the same standard—is the result a reasonable measure of relative commercial activity within the state.

What is unclear is what showing this standard can meet.[10] One method is to isolate the offending portion of the formula and show why it is not performing its intended function. In *Norfolk & Western, supra,* for example, the taxpayer showed logically why the mileage formula did not fairly predict the value of its railroad cars in Missouri (specialized rolling stock which never entered the state). And in *Wallace v. Hines,* Justice Holmes took judicial notice that North Dakota was a plains state without many railroad terminals and, therefore, concluded that the mileage formula was inappropriate. A second method is to demonstrate that other generally accepted measures of commercial activity which are more particularly suited to the taxpayer's business show that the taxpayer's actual commercial activity is

9. The point is fundamental. See, e.g., Beaman, *supra,* at 3-21. Yet it was avoided in this case by the trial court, which found that the taxpayer had not demonstrated any "unfairness" because it could not show that the receipts were being used in the apportionment formula of any other state (p. 40a). It need hardlly be said that failure to find a "multiple burden" (see Point III, *infra*) cannot, it itself, justify a finding that an apportionment is not unfair.

10. See Beaman, *supra,* at 3-17, 3-18:

> Without satisfactory standards for determining what would be *reasonable,* the court finds itself powerless to say whether or not the result is *unreasonable,* therefore, the court arrives essentially by confession of *ignoramus* at a finding that the taxpayer has failed to prove the unreasonableness of the formula. Thus, an apportionment case is usually an exercise of futility.

substantially disproportionate to the formula result. In *Norfolk & Western*, for example, the taxpayer produced evidence of a direct valuation of the railroad cars in question. In *Hans Rees' Sons*, the taxpayer provided a separate accounting of income.

If a taxpayer demonstrates both that the operation of a formula, or a particular factor, works a misapportionment by not fairly measuring activity or value, or by considering extraterritorial values, and that more appropriate gauges indicate the formula's result is substantially disproportionate to the taxpayer's actual commercial activity, then the faulty ingredient should be eliminated.[11] *Norfolk & Western, supra.*

These criteria have been met by the Appellant here. First, the relative receipts factor in the formula is intended generally to measure, if anything, the marketing activity of a taxpayer within the state or to compensate the state for providing a market to the seller. An interstate pipeline engages in relatively little marketing activity in general, and it is beyond argument that there was absolutely no New Jersey marketing activity in any way connected with the receipts derived from the deliveries to Algonquin. Indeed, the trial court determined that these receipts had no relationship to New Jersey. Further since the gas in question is ultimately delivered to other states New Jersey is not serving a function of providing Texas Eastern with a market for its product.

The Algonquin "sales" were not negotiated in New Jersey; the gas was not and could not be used in New Jersey; the FPC certificates of public convenience and necessity were not issued to meet New Jersey needs; the gas was simply transferred from one interstate pipeline

11. Nearly every state provides that the local tax administrator may make such adjustments to the formula when the formula apportionment is unfavorable to the state. See, *e.g.*, N.J. STAT. ANN. 54:10A-8.

company to another and its transmission through New Jersey, as through every other state until it reached its ultimate destination, was at high speed and under high pressure without a moment's interruption. Thus, as a measure of marketing activity in New Jersey, the "sales" and therefore the receipts are meaningless.

Second, the generally accepted formula for apportioning the business activity of an interstate pipeline is relative pipeline mileage. New Jersey itself utilizes relative pipeline mileage to apportion the interstate business activity of state regulated pipeline companies for the purpose of their franchise taxation. N.J. STAT. ANN. §§54:30-18, 58.[12] Only 2.6% of Texas Eastern's pipeline mileage is in New Jersey, a figure which is substantially disproportionate to the 9.3% which the State of New Jersey claims. The two factor property-payroll formula, which is the leading alternative to the Massachusetts formula, would apportion 2.5% of the company's commercial activity to New Jersey. See the WILLIS REPORT, *supra*, at 526-29, 562-63.[13]

Inclusion of the New Jersey destination sales in the formula results in an apportionment of less than 5%, a figure which, as stated earlier, the Appellant does not regard as constitutionally unreasonable. The doubling of that figure by addition of the Algonquin receipts is an obvious distortion. Had the gas in question moved on the very same journey through New Jersey but wholly in Texas Eastern

12. This Court has repeatedly found mileage formulas reasonable as applied to railroads, e.g., *Maine v. Grand Trunk Ry., supra.* An interstate natural gas pipeline is functionally no different from a railroad as it obtains gas from producers, ships it interstate and delivers it to local utilities for eventual consumption. Indeed, it often occurs that gas is delivered from one interstate utility to another much as goods are shipped from one railroad to another. For a mileage apportionment found reasonable with respect to bus lines, see *Central Greyhound Lines v. Mealey*, 334 U.S. 653 (1948).

13. Texas Eastern also demonstrated below that the social costs it generated locally were minimal. Obviously, the Algonquin transfers could have generated no local costs whatever.

pipes, the company's commercial activity in New Jersey, as measured by the statet's application of the formula, would be reduced by 50%. The unreasonableness of such a conclusion speaks for itself and graphically demonstrates the irrelevance of the Algonquin receipts as any true measurement of Texas Eastern's commercial activity in New Jersey.

This taxpayer makes no claim that it is constitutionally entitled to the most reasonable apportionment formula, but whatever formula is used must come to a reasonable result. Here the application of the Massachusetts formula, excluding therefrom the receipts which have no meaningful relationship to New Jersey, yields the highest return for the state consistent with reason. New Jersey's further step of including the Algonquin receipts results in the taxation of extraterritorial values and is repugnant to the Constitution.

III.

Whether the cumulative impact of successive taxation, on or measured by gross receipts in the transfer of natural gas in interstate commerce, imposes a multiple burden "on commerce."

While the record in this case does not show an instance of multiple taxation of this particular taxpayer, the Court should be alert to the dangers of multiple taxation of "commerce" when receipt directed taxes are levied upon interstate commerce As this Court stated in *General Motors Corp. v. Washington, supra:*

> However, local taxes measured by gross receipts from interstate commerce have not always faired as well. Because every state has equal rights when taxing the commerce it touches, there exists the danger that such taxes can impose cumulative burdens upon interstate transactions which are not present to local commerce. [Citations omitted] Such burdens would destroy interstate commerce and encourage the re-erection of those trade barriers which made the Commerce Clause necessary. [at 440]

The record in this case demonstrates that taxes related in great part to gross receipts are imposed both at the point of delivery to the local utility and at a point of delivery between two interstate carriers. The record also demonstrates that the gas in question is received by Texas Eastern at remote delivery points in the Southwest. As illustrative of the course this gas takes in its interstate journey from the producing fields to the consumer we note that the gas ultimately destined for use in Massachusetts in this case experiences seven separate carrier transfers enroute. The gas is delivered first to an interstate pipeline (United). This pipeline delivers the gas in Louisiana to Texas Eastern. Texas Eastern delivers the gas again in Louisiana to the Texas Gas Transmission Company. Texas Gas Transmission Company then redelivers it back to Texas Eastern in Ohio. Texas Eastern then delivers the gas to Algonquin. Algonquin delivers it to Boston Gas in Massachusetts. Boston Gas finally delivers it to the public. At every stage of this transaction a tax related to gross receipts is imposed upon the transfer of the same gas from one carrier to another, until it reaches its final destination.

While the concept of "multiple burdens" more obviously has been employed where a taxpayer shows that it has been subjected to a multiple burden, the multiple burdening of *commerce* is socially the more significant phenomenon. Here, the ultimate burden of the increased cost of carrying the gas to its ultimate destination is reflected in the rate base of a regulated company such as Texas Eastern

and therefore borne by the consumer. It need hardly be added that particularly in the case of fuels such as natural gas the consumer has in recent years been faced with spiraling costs. In this context multiple taxation of natural gas as it moves from source to user is especially repugnant. A significant additional cost is added which is unrelated to the true cost of producing and transporting natural gas.

It is true that so long as there is a lack of uniformity of state laws under which taxes (by formula or otherwise) are imposed upon the various carriers of the gas as it moves in interstate commerce, there can be no assurance that multiple taxation will not continue to occur. It is also true that it may not be within the province of this Court to impose such a uniform system of taxation. But what this Court can do is to require that whatever formula a particular state may utilize produce a result which fairly measures the commercial activity of the particular taxpayer within that particular state. It is submitted that New Jersey has exacted a levy far beyond its fair share.

It is also clear that New Jersey has breached fundamental constitutional concepts of interstate commerce long recognized by this Court and well summarized in *Michigan-Wisconsin Pipeline Co. v. Calvert*, 347 U.S. 157 (1954):

> It is now well settled that a tax imposed on local activity related to interstate commerce is valid if, and only if, the local activity is not such an integral part of the interstate process, the flow of commerce, that it cannot be realistically separated from it . . . And if a genuine separation of the taxed local activity from the interstate process is impossible, it is more likely that other states through which the commerce passes or into which it flows can with equal right impose a similar levy on the goods with the net effect of prejudicing or unduly burdening commerce [347 U.S. at 166].
>
> • • •
>
> [The tax] would "permit a multiple burden upon that commerce," . . . for if Texas may impose this "first taking" tax . . . then Michigan and the other recipient states have at least equal right to tax the first taking or "unloading" from the pipeline of the same gas when it arrives for distribution. Oklahoma might then seek to tax the first taking of the gas as it crossed into that State. The net effect would be substantially to resurrect the customs barriers which the Commerce Clause was designed to eliminate. [347 U.S., at 190].

In this case New Jersey's exaction of a tax based upon a transfer of gas found to be an "integral part of the interstate process" and with respect to which New Jersey is "only remotely and incidentally connected" not only clearly results in an excessive apportionment as to that state, but also, if left uncorrected, will encourage other states to assess taxes based upon extraterritorial values.

SUMMARY OF ARGUMENT

A fair formula unreasonably applied may produce an unconstitutional result. In the absence of effective direction from this Court, state taxing officials, under the guise of mechanical application of generally acceptable formulas, have it in their power to assess taxes which may reflect a wholly distorted estimation of a particular taxpayer's commercial activity within the state. The time is ripe and the circumstances appropriate for this Court to make an affirmative determination that the results of the application of such formulas are subject to the same scrutiny under the Commerce Clause of the United States Constitution, as the formulas themselves.

Here, New Jersey's unreasonable inclusion of Appellant's receipts from transfers of gas moving through the state in interstate commerce unconstitutionally distorts the measurement of Texas Eastern's commercial activity in New Jersey. The inclusion of such receipts virtually doubles the formula's measurement of Appellant's presence, notwithstanding the fact that the transfers had only an incidental relationship to New Jersey as the trial Court subseqently found.

Since the natural gas in question may be subjected to multiple tax burdens on its route from the producing fields to the consumer, and since it is the consumer who ultimately bears the burden of the taxes, it is especially important that it be known that this Court will scrutinize the results of a state's taxing formula to assure that it reflects a substantially fair approximation of an interstate taxpayer's commercial activity within the state.

CONCLUSION

For the foregoing reasons, probable jurisdiction should be noted.

Respectfully submitted,

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APPENDIX

STIPULATION OF FACTS

(Filed September 15, 1972)

The parties hereto do hereby stipulate and agree to the facts contained in the annexed Stipulation of Facts for the purposes of, and in connection with, the above-captioned matter: *provided, however,* that: (1) Respondent reserves the right and option to object to the relevancy of the facts set forth in Paragraphs D(1), D(2) and D(3) of said annexed Stipulation of Facts; and (2) both parties reserve the right and option to introduce evidence not inconsistent with the stipulations contained herein.

JEFFERS and DILLON
Attorneys for Petitioner

By /s/ Robert J. Del Tufo
ROBERT J. DEL TUFO
A Member of the Firm

GEORGE F. KUGLER, JR.,
Attorney General of
New Jersey,
Attorney for Respondent

By /s/ Harry Haushalter
HARRY HAUSHALTER
Deputy Attorney General

Preliminary

1. Pursuant to *N.J.S.A.* 54:10A-8 and Regulation 16:10-4.300, Texas Eastern Transmission Corporation (hereinafter "Texas Eastern") applied to the Director of the Division of Taxation to adjust the business allocation factor used in the determination of its 1967 assessment under the Corporation Business Tax.

Without the adjustment requested by Texas Eastern, the 1967 assessment of the Corporation Business Tax upon Texas Eastern produced:

(a) a business allocation factor of 9.2860%, being the average of a 22.8380% allocation of "receipts," a 4.0412% allocation of "assets" and a 0.9789% allocation of "payroll";

(b) a tax liability of $174,173.58.

2. The adjustment sought by Texas Eastern, pursuant to the application referred to in Paragraph 1, above, involved the receipts portion of the formula and requested elimination of receipts received from Algonquin Gas Transmission Company (hereinafter "Algonquin") for gas transferred to Algonquin and transported by Algonquin to other States (See Paragraphs B(3), B(4) and B(5), infra)—i.e. the sum of $49,042,131.00. If the adjustment requested by Texas Eastern was granted in its entirety, the 1967 assessment of the Corporation Business Tax upon Texas Eastern would produce:

(a) a business allocation factor of 4.9934%, being the average of a 9.9602% allocation of "receipts," a 4.0412% allocation of "assets" and a 0.9789% allocation of "payroll";

(b) a tax liability of $93,659.09.

3. The amount of taxes paid by Texas Eastern under the Corporation Business Tax Act for the year 1966 was $66,592.77.

4. Submitted contemporaneously herewith, as Joint Exhibits 1 and 2, are copies of the 1966 and 1967 Corporation Business Tax Returns of Texas Eastern.

A. Corporate Status

1. Texas Eastern is a corporation duly organized under the laws of the State of Delaware, having its principal offices at Houston, Texas.

2. Algonquin is a corporation duly organized under the laws of the State of Delaware, having its principal offices in Boston, Massachusetts.

3. Both Texas Eastern and Algonquin are interstate natural gas companies within the meaning of the federal "Natural Gas Act" (52 Stat. 82 (1938), 15 U.S.C. §717 *et seq.*) and, as such, are regulated by the Federal Power Commission (hereinafter "FPC") with respect to the transportation and sale for resale of natural gas in interstate commerce. Under the terms of the Act, the FPC has exclusive jurisdiction over all aspects of such transportation and sale for resale of natural gas by both Texas Eastern and Algonquin. The FPC's prior approval, under a certificate of public convenience and necessity, is a prerequisite to the conduct of such activities as well as to the construction or acquisition of transportation facilities. The FPC also has exclusive jurisdiction over rates, charges and earnings.

B. Operations

1. Texas Eastern transports natural gas by pipeline from producing fields located principally in Texas and Louisiana to markets in the Midwest and Northeast United States. Texas Eastern owns several of these producing fields and gas produced from them is commingled with gas purchased from others in the various producing states. The gas

produced by Texas Eastern from fields owned by it constitutes a minor portion of Texas Eastern's system gas supplies and most of the gas is purchased from independent producers. Texas Eastern has ownership rights over such gas upon entry of the gas into its interstate transmission system for transport. During 1967, Texas Eastern was licensed by the FPC to make deliveries of natural gas in the following states:

New Jersey	Arkansas
New York	Kentucky
Indiana	Tennessee
Ohio	Alabama
Illinois	Mississippi
Missouri	Louisiana
Pennsylvania	Texas

2. In 1967, Texas Eastern transferred natural gas (88,512,234 MCF) from its interstate pipeline system to three New Jersey public utliities (Public Service Electric and Gas Company, New Jersey Natural Gas Company, and Elizabethtown Gas Company) for distribution and sale by these utilities to consumers in New Jersey. The transfer to each utility constituted one element of a wholesale sale for resale of natural gas in interstate commerce under the exclusive jurisdiction of the FPC. The New Jersey utilities in turn supplied the gas only to New Jersey residents for their consumption. The pipelines of the New Jersey utilities are connected with the pipelines of Texas Eastern at the delivery points. Natural gas flows from the high pressure pipelines of Texas Eastern without interruption into equipment which reduces the flowing pressure of the gas to a sufficient level so as to permit it to flow into the distribution facilities of the New Jersey utilities and to be capable of consumer distribution. Measurement equipment records the volume flowing from Texas Eastern's high pressure pipeline system into the facilities of the New Jersey utilities.

3. In 1967, a total of 116,135,686 MCF of natural gas was transferred at high pressure (750 psig) from the interstate pipeline system of Texas Eastern into the interstate pipeline system of Algonquin without interruption in movement through measurement and recording equipment at measuring and regulating stations of Texas Eastern located in New Jersey and continued its flow to Algonquin's customers. This equipment was used to measure the quantity of natural gas so transferred. (73,164,596 MCF at Lambertville Station, West Amwell Township, Hunterdon County, New Jersey and 42,971,090 MCF at Hanover Station, Hanover Township, Morris County, New Jersey). The transfer of gas from Texas Eastern to Algonquin constituted one element of the wholesale for resale of natural gas in interstate commerce by Texas Eastern to Algonquin under the exclusive jurisdiction of the FPC. The pipelines of Texas Eastern are connected with the pipelines of Algonquin at the points of transfer. Measuring equipment at the points of transfer automatically measure and record the volume of natural gas flowing from Texas Eastern's pipelines into Algonquin's pipelines. This equipment essentially consists of a calibrated orifice plate and instruments which continuously record the pressure of the gas flowing through the orifice on each side of the orifice.

In return for the 116,135,686 MCF of natural gas transferred by Texas Eastern to Algonquin in 1967, Texas Eastern received the total sum of $49,601,205.04 from Algonquin. These receipts have not been allocated by any other State to that State for purposes of determining the allocation formula for computing taxes in that State. Of these

receipts, the sum of $559,074.04 is not, and was not, included in the adjustment sought by Texas Eastern for the 1967 tax year. This $559,074.04 portion of the receipts is from the 1,309,000 MCF of gas transferred to Algonquin which, as hereinafter referred to in Paragraph B(4), was in turn transferred by Algonquin to New Jersey Natual Gas Company for in-State consumption.

4. Approximately 99% (114,826,686 MCF) of the natural gas so transferred was destined for other states and remained in continuous uninterrupted flow at high pressure out of New Jersey in the interstate pipeline system of Algonquin to distributors in the States of Massachusetts, Rhode Island, Connecticut and New York (the major portion thereof (approximately 95%) moving to the above-mentioned three New England States). Approximately 1% of the natural gas so transferred by Texas Eastern to Algonquin was delivered by Algonquin in the State of New Jersey, 1,309,000 MCF having been transferred by Algonquin to New Jersey Natural Gas Company for distribution and sale by that utility to consumers in New Jersey. During 1967, Algonquin was licensed by the FPC to make deliveries of natural gas in the following States:

New York
New Jersey
Massachusetts
Rhode Island
Connecticut

The total amount of receipts received by Algonquin during 1967 for the deliveries of the gas to its customers in New York, Massachusetts, Rhode Island and Connecticut was $65,120,457.81.

5. Since its inception, Algonquin has principally served markets in the above-mentioned three New England States and has received its entire gas supply from Texas Eastern pursuant to various FPC certificates of public convenience and necessity authorizing both the transfer of natural gas by Texas Eastern to Algonquin and the transfer of that gas by Algonquin to distributors in the States of destination to meet consumer needs.

Prior to its 1951 commencement of service, Algonquin and Tennessee Gas Transmission Company (hereinafter "Tennessee") had each sought the exclusive FPC license to service the New England area. Instead, the FPC divided the New England Service area between Algonquin and Tennessee, a division which still existed as of the 1967 tax year. No other natural gas company has been, or is, licensed to service that area.

As indicated above, Texas Eastern has always been Algonquin's sole supplier of the natural gas which Algonquin in turn delivers to its customers. The FPC does not preclude interstate gas carriers such as Algonquin and Texas Eastern from negotiating among themselves for the supplying of gas, with the FPC giving approval to any final agreement. Algonquin thus could have negotiated with other interstate gas carriers for its gas supply. However, since 1951 Algonquin has had connecting pipeline facilities with Texas Eastern for the delivery of natural gas and Texas Eastern has had a sufficient gas supply to service Algonquin's requirements. It would thus have been both unnecessary and uneconomical for Algonquin to seek new sources of supply with the attendant need to construct new pipelines and related facilities required to establish new delivery points with the supplier; prior FPC approval of any new supply source or attendant new construction is legally required under a certificate of public convenience and necessity deeming both to be in the public interest.

In order for Texas Eastern to obtain the required approval from the FPC to sell a specified amount of natural gas to a customer such as Algonquin, it must be established to the satisfaction of the FPC that such a sale is required by the public convenience and necessity. For that reason, the FPC has always been included in the initial contract negotiations between Texas Eastern and Algonquin. In addition, the form and contents of the relevant contracts, the rate schedules, and general terms and conditions incorporated therein must conform to the Rules and Regulations of the Federal Power Commission and be approved by it under Section 4 of the Natural Gas Act.

Under the Commission's Rules and Regulations a sales contract (service agreement) may not be modified by a separate agreement amending the sales contract, but must be superseded by a new service agreement. Since Texas Eastern has sold additional quantities of natural gas to Algonquin practically every year since it started selling natural gas to Algonquin in 1951, many superseding service agreements have been executed by the parties to provide for the sale of such additional quantities of gas. In this connection, the superseding service agreements under which sales were made during 1967 were negotiated during 1966.

The procedure for gaining Federal Power Commission approval for Texas Eastern to sell any quantity of natural gas for resale to Algonquin as provided in a service agreement between them is for Texas Eastern to file an application for a certificate of public convenience and necessity seeking authorization to make such sale and for Algonquin to file a companion application for a certificate of public convenience and necessity seeking authorization to sell such additional quantities of natural gas for resale to those of its customers which enter into service agreements with Algonquin. In making any certification application it is

necessary to specify the quantities of natural gas to be distributed to the general public in each local market area by the local distributing company and to submit market data establishing the need of the local distribution company for such quantities of natural gas. Since the gas sold by Texas Eastern to Algonquin is not distributed to the general public at the point of delivery to Algonquin but is transferred from one interstate pipeline to another, the certificate applications of Texas Eastern and Algonquin are interdependent and both depend upon the need of Algonquin's local distribution companies for additional quantities of natural gas to meet the requirements of the public served by them. In authorizing the companion certificate applications, the Commission authorizes Texas Eastern to sell additional quantities of natural gas to Algonquin and Algonquin to sell allocated portions of such quantities of natural gas to Algonquin's local distribution customers. All of the natural gas thus authorized to be sold by Texas Eastern to Algonquin is, in turn, authorized to be sold by Algonquin to its aforesaid local distributing customers, except such minor portions thereof which are required by Algonquin to operate its interstate pipeline system. If any additional facilities are required to be constructed by Texas Eastern and by Algonquin in order to make the additional sales, each of them must also apply for and receive certificate authorization to construct and operate such additional facilities. The procedure also includes the filing of the agreements with the Commission and receiving approval from the Commission for such agreements to be on file and in effect with the Commission under Section 4 of the Natural Gas Act.

6. All of the 1967 shipments and transfers of natural gas mentioned in Paragraphs B(2), (3) and (4), above, both by Texas Eastern and by Algonquin were similarly made pursuant to authorizations of the FPC under various

certificates of public convenience and necessity and accordingly such shipments and transfers could not be modified by either Texas Eastern or Algonquin.

Service contracts covering the 1967 deliveries of natural gas from Texas Eastern to Algonquin were negotiated and executed outside of New Jersey and were filed with the FPC in Washington, D. C. Mr. Walter E. Caine and Mr. Jack E. Bixby, Vice Presidents of Texas Eastern, were the negotiating parties to the agreements on behalf of Texas Eastern and John B. Thorn, Vice President of Algonquin, was the negotiating party on behalf of Algonquin. All negotiations were conducted between Houston, Texas and Boston, Massachusetts. Applicable rate schedules and tariffs were approved by the FPC and were filed with it in Washington, D. C. The natural gas was dispatched by direction from Shreveport, Louisiana; billing was also from Shreveport, while payment was made from Boston, Massachusetts.

C. Facilities

1. During 1967, Texas Eastern's interstate natural gas system comprised 8184.1 miles of pipeline, along with appurtenant measuring and regulating, compressor and microwave facilities and related equipment, located in 16 States.[1] It maintained extensive office facilities both in Houston and in Shreveport, Louisiana.

2. During 1967, Texas Eastern had no permanent office facility in New Jersey. Of the system mentioned in paragraph C(1), above, its total New Jersey facilities consisted of: (a) 209.6 miles of underground pipeline; (b) a maintenance office in Linden; (c) 29 employees, all for the purpose of maintaining and operating its pipeline system, and commanding a total payroll of $214,376.28; (d) various measuring and regulating, compressor and microwave facilities and related equipment necessary and appurtenant to the operation of its pipeline system.

1. The 8184.1 figure covers only natural gas transmission lines. It does not include gas pipelines used in connection with storage or gathering lines used to secure gas at Southern producing fields.
The figure also does not include 2610.1 miles of products pipeline (2521.7 miles owned by Texas Eastern, 40.4 miles which it leases and 48 miles in joint ownership). None of these products pipelines are located in New Jersey.

3. During 1967, Algonquin's interstate natural gas transmission system comprised 829.7 miles of pipeline, along with appurtenant measuring and regulating and compressor stations located in 5 States. Of this amount, 90.4 miles were located in New Jersey consisting of: a 26-inch pipeline running from Texas Eastern's Lambertville Measuring and Regulating Station 26 (located near Lambertville just east of the Delaware River), running in a northeasterly direction through Hunterdon, Somerset, Morris and Passaic Counties, and leaving New Jersey and crossing the New York line at a point near Suffern; and a parallel 30-inch pipeline running from Texas Eastern's Hanover Measuring and Regulating Station in Hanover Township, Morris County.

NOTE: *Respondent reserves the right and option to object to the relevancy of the facts set forth in Paragraphs D(1), D(2) and D(3), below.*

D. Taxes and Miscellaneous

1. For the year 1967, Texas Eastern: (a) paid a total of $750,189.83 in ad valorem property taxes in New Jersey under total assessments of $17,541,321.00 levied upon its pipeline properties, appurtenant lands and measuring and regulating and compressor facilities, and related equipment necessary and appurtenant to the operation of its pipelines;

(b) included, in the "receipts" portion of the business allocation factor used in the determination of its assessment for that year under the New Jersey Corporation Business Tax Act, the revenues it received from the New Jersey public utilities described in Paragraph B(2), above, for the transfer to them of the natural gas described in Paragraph B(2), above, as well as the revenues from the transfer to Algonquin described in Paragraph B(3), above; (c) included, in the "assets" portion of said business allocation factor, the same properties upon which ad valorum property taxes were assessed and paid; (d) paid a total of $1,059.00 of miscellaneous other State and local taxes in New Jersey.

2. For the year 1967, Algonquin: (a) paid ad valorem property taxes in New Jersey upon its pipeline properties as well as upon appurtenant measuring and regulating and compressor facilities and related equipment involved in, and necessary to, operation of its pipeline; (b) included, in the "receipts" portion of the business allocation factor used in the determination of its assessment for that year under the New Jersey Corporation Business Tax Act, the revenues it received from New Jersey Natural Gas Company for the transfer to the latter of the 1,309,000 MCF of natural gas described in Paragraph B(4), above; (c) included, in the "assets" portion of said business allocation factor, the same properties upon which ad valorem property taxes were assessed and paid; (d) included, in the computation of assessments of income and franchise taxes in the States of New York, Connecticut, Massachusetts, and Rhode Island, revenues it received from distributors in those States for the delivery of the 114,826,686 MCF of natural gas described in Paragraph B(4), above, and paid the following income and franchise taxes in those States: New York—$32,256.00; Connecticut—$96,049.00; Massachusetts—$41,250.00; and Rhode Island—$19,485.00.

3. For the year 1967, New Jersey Natural Gas Company, Public Service Electric & Gas Company, and Elizabethtown Gas Company paid a tax assessed pursuant to *N.J.S.A.* 50:30A-49, *et seq.*, upon the gross receipts each received from consumers upon the resale to them at retail of the natural gas transferred to them by both Texas Eastern and Algonquin as described in Paragraph B(2) and Paragraph B(4), above.

OPINION OF THE DIVISION OF TAXATION
(Filed June 5, 1975)

Appearances:

JEFFERS & DILLON, ESQS.,
By: Robert J. Del Tufo, Esq.,
For the Petitioner.

GEORGE F. KUGLER, JR., ATTORNEY GENERAL,
BY: Harry Haushalter, Deputy Attorney General,
For the Respondent.

MOTT, J.:

This matter has been submitted to the division for determination pursuant to the following stipulation of facts:

1. Pursuant to *N.J.S.A.* 54:10A-8 and Regulation 16:10-4.300, Texas Eastern Transmission Corporation (hereinafter "Texas Eastern") applied to the Director of the Division of Taxation to adjust the business allocation factor used in the determination of its 1967 assessment under the Corporation Business Tax.

Without the adjustment requested by Texas Eastern, the 1967 assessment of the Corporation Business Tax upon Texas Eastern produced:

(a) a business allocation factor of 9.2860%, being the average of a 22.8380% allocation of "receipts," a 4.0412% allocation of "assets" and a 0.9789% allocation of "payroll";
(b) a tax liability of $174,173.58.

2. The adjustment sought by Texas Eastern, involved the receipts portion of the formula and requested elimination of receipts received from Algonquin Gas Transmission Company (hereinafter "Algonquin") for gas transferred to Algonquin and transported by Algonquin to other states the sum of $49,042,131.00. If the adjustment requested by

Texas Eastern was granted in its entirety, the 1967 assessment of the Corporation Business Tax upon Texas Eastern would produce:

(a) a business allocation factor of 4.9934%, being the average of 9.9602% allocation of "receipts," a 4.0412% allocation of "assets" and a 0.9789% allocation of "Payroll";
(b) a tax liability of $93,659.09.

3. The amount of taxes paid by Texas Eastern under the Corporation Business Tax Act for the year 1966 was $66,-592.77.

Texas Eastern is a corporation duly organized under the laws of the State of Delaware, having its principal offices at Houston, Texas.

Algonquin is a corporation duly organized under the laws of the State of Delaware, having its principal offices in Boston, Massachusetts.

Both Texas Eastern and Algonquin are interstate natural gas companies within the meaning of the federal "Natural Gas Act" (52 Stat. 82 (1938), 15 U.S.A. 717 *et seq.*) and, as such, are regulated by the Federal Power Commission (hereinafter "FPC") with respect to the transportation and sale for resale of natural gas in interstate commerce. Under the terms of the Act, the FPC has exclusive jurisdiction over all aspects of such transportation and sale for resale of natural gas by both Texas Eastern and Algonquin. The FPC's prior approval, under a certificate of public convenience and necessity, is a prerequisite to the conduct of such activities as well as to the construction or acquisition of transportation facilities. The FPC also has exclusive jurisdiction over rates, charges and earnings.

Texas Eastern transports natural gas by pipeline from producing fields located principally in Texas and Louisiana to markets in the Midwest and Northeast United States.

Texas Eastern owns several of these producing fields and gas produced from them is commingled with gas purchased from others in the various producing states. The gas produced by Texas Eastern from fields owned by it constitutes a minor portion of Texas Eastern's system gas supplies and most of the gas is purchased from independent producers. Texas Eastern has ownership rights over such gas upon entry of the gas into its interstate transmission system for transport. During 1967, Texas Eastern was licensed by the FPC to make deliveries of natural gas in the following states:

New Jersey	New York	Arkansas
Pennsylvania	Indiana	Kentucky
Ohio	Illinois	Tennessee
Missouri	Alabama	Mississippi
Louisiana	Texas	

In 1967, Texas Eastern transferred natural gas (88,512,234 MCF) from its interstate pipeline system to three New Jersey public utilities (Public Service Electric and Gas Company, New Jersey Natural Gas Company and Elizabethtown Gas Company) for distribution and sale by these utilities to consumers in New Jersey. The transfer to each utility constituted one element of a wholesale sale for resale of natural gas in interstate commerce under the exclusive jurisdiction of the FPC. The New Jersey utilities in turn supplied the gas only to New Jersey residents for their consumption. The pipelines of the New Jersey utilities are connected with the pipelines of Texas Eastern at the delivery points. Natural gas flows from the high pressure pipelines of Texas Eastern without interruption into equipment which reduces the flowing pressure of the gas to a sufficient level so as to permit it to flow into the distribution facilities of the New Jersey utilities and to be

capable of consumer distribution. Measurement equipment records the volume flowing from Texas Eastern's high pressure pipeline system into the facilities of the New Jersey utilities.

In 1967, a total of 116,135,686 MCF of natural gas was transferred at high pressure (750 psig) from the interstate pipeline system of Texas Eastern into the interstate pipeline system of Algonquin without interruption in movement through measurement and recording equipment at measuring and regulating stations of Texas Eastern located in New Jersey and continued its flow to Algonquin's customers. This equipment was used to measure the quantity of natural gas so transfererd. (73,164,596 MCF at Lambertville Station, West Amwell Township, Hunterdon County, New Jersey and 42,971,090 MCF at Hanover Station, Hanover Township, Morris County, New Jersey). The transfer of gas from Texas Eastern to Algonquin constituted one element of the wholesale for resale of natural gas in interstate commerce by Texas Eastern to Algonquin under the exclusive jurisdiction of the FPC. The pipelines of Texas Eastern are connected with the pipelines of Algonquin at the points of transfer. Measuring equipment at the point of transfer automatically measure and record the volume of natural gas flowing from Texas Eastern's pipelines into Algonquin's pipelines. This equipment essentially consists of a calibrated orifice plate and instruments which continuously record the pressure of the gas flowing through the orifice on each side of the orifice.

In return for the 116,135,686 MCF of natural gas transferred by Texas Eastern to Algonquin in 1967, Texas Eastern received the total sum of $49,601,205.04 from Algonquin. These receipts have not been allocated by any other state to that State for purposes of determining the allocation formula for computing taxes in that State. Of these

receipts, the sum of $559,074.04 is not, and was not, included in the adjustment sought by Texas Eastern for the 1967 tax year. This $559,074.04 portion of the receipts is from the 1,309,000 MCF of gas transferred to Algonquin which, was in turn transferred by Algonquin to New Jersey Natural Gas Company for in-State consumption.

Approximately 99% (114,826,686 MCF) of the natural gas so transferred was destined for other states and remained in continuous uninterrupted flow at high pressure out of New Jersey in the interstate pipeline system of Algonquin to distributors in the States of Massachusetts, Rhode Island, Connecticut and New York (the major portion thereof (approximately 95%) moving to the above-mentioned three New England States). Approximately 1% of the natural gas so transferred by Texas Eastern to Algonquin was delivered by Algonquin in the State of New Jersey, 1,309,000 MCF having been transferred by Algonquin to New Jersey Natural Gas Company for distribution and sale by that utility to consumers in New Jersey. During 1967, Algonquin was licensed by the FPC to make deliveries of natural gas in the following States:

New York	New Jersey	Rhode Island
Massachusetts	Connecticut	

The total amount of receipts received by Algonquin during 1967 for the deliveries of the gas to its customers in New York, Massachusetts, Rhode Island and Connecticut was $65,120,457.81.

Since its inception, Algonquin has principally served markets in the above-mentioned three New England States and has received its entire gas supply from Texas Eastern pursuant to various PFC certificates of public convenience and necessity authorizing both the transfer of natural gas

by Texas Eastern to Algonquin and the transfer of that gas by Algonquin to distributors in the States of destination to meet consumer needs.

Prior to its 1951 commencement of service, Algonquin and Tennessee Gas Transmission Company (hereinafter "Tennessee") had each sought the exclusive FPC license to service the New England area. Instead, the FPC divided the New England Service area between Algonquin and Tennessee, a division which still existed as of the 1967 tax year. No other natural gas company has been, or is, licensed to service that area.

As indicated above, Texas Eastern has always been Algonquin's sole supplier of the natural gas which Algonquin in turn delivers to its customers. The FPC does not preclude interstate gas carriers such as Algonquin and Texas Eastern from negotiating among themselves for the supplying of gas, with the FPC giving approval to any final agreement Algonquin thus could have negotiated with other interstate gas carriers for its gas supply. However, since 1951 Algonquin has had connecting pipeline facilities with Texas Eastern for the delivery of natural gas and Texas Eastern has had a sufficient gas supply to service Algonquin's requirements. It would thus have been both unnecessary and uneconomical for Algonquin to seek new sources of supply with the attendant need to establish new delivery point with the supplier; prior FPC approval of any new supply source or attendant new construction is legally required under a certificate of public convenience and necessity deeming both to be in the public interest.

In order for Texas Eastern to obtain the required approval from the FPC to sell a specified amount of natural gas to a customer such as Algonquin, it must be established to the satisfaction of the FPC that such a sale is required by the public convenience and necessity. For that reason,

the FPC has always been included in the initial contract negotiations between Texas Eastern and Algonquin. In addition, the form and contents of the relevant contracts, the rate schedules, and general terms and conditions incorporated therein must conform to the Rules and Regulations of the Federal Power Commission and be approved by it under Section 4 of the Natural Gas Act.

Under the Commission's Rules and Regulations a sales contract (service agreement) may not be modified by a separate agreement amending the sales contract, but must be superseded by a new service agreement. Since Texas Eastern has sold additional quantities of natural gas to Algonquin practically every year since it started selling natural gas to Algonquin in 1951, many superseding service agreements have been executed by the parties to provide for the sale of such additional quantities of gas. In this connection, the superseding service agreements under which sales were made during 1967 were negotiated during 1966.

The procedure for gaining Federal Power Commission approval for Texas Eastern to sell any quantity of natural gas for resale to Algonquin as provided in a service agreement between them is for Texas Eastern to file an application for a certificate of public convenience and necessity seeking authorization to make such sale and for Algonquin to file a companion application for a certificate of public convenience and necessity seeking authorization to sell such additional quantities of natural gas for resale to those of its customers which enter into service agreements with Algonquin. In making any certification application it is necessary to specify the quantities of natural gas to be distributed to the general public in each local market area by the local distributing company and to submit market data establishing the need of the local distribution company for such quantities of natural gas. Since the gas sold by Texas Eastern to Algonquin is not distributed to the general public at the point of delivery to Algonquin but is transferred from one interstate pipeline to another, the certificate applications of Texas Eastern and Algonquin are interdependent and both depend upon the need of Algonquin's local distribution companies for additional quantities of natural gas to meet the requirements of the public served by them. In authorizing the companion certificate applications, the Commission authorizes Texas Eastern to sell additional quantities of natural gas to Algonquin and Algonquin to sell allocated portions of such quantities of natural gas to Algonquin's local distribution customers. All of the natural gas thus authorized to be sold by Texas Eastern to Algonquin, is, in turn, authorized to be sold by Algonquin to is aforesaid local distributing customers, except such minor portions thereof which are required by Algonquin to operate its interstate pipeline system. If any additional facilities are required to be constructed by Texas Eastern and by Algonquin in order to make the additional sales, each of them must also apply for and receive certificate authorization to construct and operate such additional facilities. The procedure also includes the filing of the agreements with the Commission and receiving approval from the Commission for such agreements to be on file and in effect with the Commission under Section 4 of the Natural Gas Act.

All of the 1967 shipments and transfers of natural gas mentioned above, both by Texas Eastern and by Algonquin were similarly made pursuant to authorizations of the FPC under various certificates of public convenience and necessity and accordingly such shipments and transfers could not be modified by either Texas Eastern or Algonquin.

Service contracts covering the 1967 deliveries of natural gas from Texas Eastern to Algonquin were negotiated and executed outside of New Jersey and were filed with the FPC in Washington, D.C. Mr. Walter E. Caine and Mr. Jack E. Bixby, Vice Presidents of Texas Eastern, were the negotiating parties to the agreements on behalf of Texas Eastern and John B. Thorn, Vice President of Algonquin, was the negotiating party on behalf of Algonquin. All negotiations were conducted between Houston, Texas and Boston, Massachusetts. Applicable rate schedules and tariffs were approved by the FPC and were filed with it in Washington, D.C. The natural gas was dispatched by direction from Shreveport, Louisiana; billing was also from Shreveport, while payment was made from Boston, Massachusetts.

During 1967, Texas Eastern's interstate system comprised 8184.1 miles of natural gas transmission pipeline, along with appurtenant measuring and regulating, compressor and microwave facilities and related equipment, located in 16 States. It maintained extensive office facilities both in Houston and in Shreveport, Louisiana.

During 1967, Texas Eastern had no permanent office facility in New Jersey. Of the system mentioned above, its total New Jersey facilities consisted of: (a) 209.6 miles of underground pipeline; (b) a maintenance office in Linden; (c) 29 employees, all for the purpose of maintaining and operating its pipeline system, and commanded a total payroll of $214,376.28; (d) various measuring and regulating compressor and microwave facilities and related equipment necessary and appurtenant to the operation of its pipeline system.

During 1967, Algonquin's interstate natural gas transmission system comprised 829.7 miles of pipeline, along with appurtenant measuring and regulating and compressor stations located in 5 States. Of this amount, 90.4 miles were located in New Jersey consisting of: a 26-inch pipeline running from Texas Eastern's Lambertville Measuring and Regulating Station 26 (located near Lambertville just each of the Delaware River), and running in a northeasterly direction through Hunterdon, Somerset, Morris and Passaic Counties, and leaving New Jersey and crossing the New York line at a point near Suffern; and a parallel 30-inch pipeline running from Texas Eastern's Hanover Measuring and Regulating Station in Hanover Township, Morris County.

The following facts were stipulated subject to the State objecting as to the relevancy:

For the year 1967, Texas Eastern: (a) paid a total of $701,603,46 in ad valorem property taxes in New Jersey under total assessments of $14,746,474.00 levied upon its pipeline properties, appurtenant lands and measuring and regulating and compressor facilities, and related equipment necessary and appurtenant to the operation of its pipelines; (b) included, in the "receipts" portion of the business allocation factor used in the determination of its assessment for that year under the New Jersey Corporation Business Tax Act, the revenues it received from the New Jersey public utilities described above, for the transfer to them of the natural gas, as well as the revenues from the transfer to Algonquin of gas sold for use in New Jersey; (c) included, in the "Assets" portion of said business allocation factor, the same properties upon which ad valorem property taxes were assessed and paid; (d) paid a total of $1,059.00 of miscellaneous other State and local taxes in New Jersey.

For the year 1967, Algonquin: (a) paid ad valorem property taxes in New Jersey upon its pipeline properties as well as upon appurtenant measuring and regulating and

compressor facilities and related equipment involved in, and necessary to, operation of its pipeline; (b) included, in the "receipts" portion of the business allocation factor used in the determination of its assessment for that year under the New Jersey Corporation Business Tax Act, the revenues it received from New Jersey Natural Gas Company for the transfer to the latter of the 1,309,000 MCF of natural gas; (c) included, in the "assets" portion of said business allocation factor, the same properties upon which ad valorem property taxes were assessed and paid; (d) included, in the computation of assessments of income and franchise taxes in the States of New Jersey, Connecticut, Massachusetts, and Rhode Island, revenues it received from distributors in those States for the delivery of the 114,826,686 MCF of natural gas, and paid the following income and franchise taxes in those States: New York—$32,256.00; Connecticut—$96,049.00; Massachusetts—$41,250.00; and Rhode Island—$19,485.00.

For the year 1967, New Jersey Natural Gas Company, Public Service Electric & Gas Company and Elizabethtown Gas Company paid a tax assessed pursuant to *N.J.S.A.* 50:30A-49, *et seq.*, upon the gross receipts each received from consumers upon the resale to them at retail of the natural gas transferred to them by both Texas Eastern and Algonquin.

The issue of the evidential relevancy of these facts must be resolved in favor of the taxpayer, in that any tax imposed must fairly relate to the value of in-state use of the corporate franchise and may not be levied upon operations which are of an interstate nature. *General Motors Corp. v. State of Washington* (377 U.S. 436); *General Motors Corporation v. District of Columbia* (380 U.S. 553); *F. W. Woolworth Co. v. Director of Division of Taxation,* 45 N.J. 466 (1965); *Roadway Express, Inc. et al v. Director, Division of Taxation,* 50 N.J. 471 (1967).

In accordance with pertinent regulations, Texas Eastern prepared its return, computed and paid the tax, without regard to the requested adjustment. It also prepared and filed a detailed adjustment application which included a recalculation of the apportionment formula and a computation of the amount of tax due under it. Elimination of the interstate revenues involved reduced allocated receipts to 9.9602% and, concomitantly, the business allocation factor to 4.9934%.

The unadjusted tax paid by Texas Eastern was $174,173.58. If the adjustment requested had been granted in full, the tax liability would have amounted to $93,659.09, a sum in excess of the $66,592.77 paid by Texas Eastern in 1966.

Director Kingsley refused to exercise his adjustment authority either in whole or in part. He denied Texas Eastern's application in its entirety. This appeal was taken from that action.

In its claim for an adjustment for 1967, Texas Eastern requested that the receipts from the sale of natural gas sold to Algonquin which was destined for delivery into other states be eliminated from being used in the numerator of the receipts portion of the business allocation factor for purposes of measuring the amount of the taxpayer's net worth and net income allocatable to this State. Thus Texas Eastern did not contest the validity of allocating to New Jersey the receipts from the direct sales to the three New Jersey public utilities and the receipts from the sale of the 1,309,000 MCF to Algonquin which were, in turn, resold to the New Jersey Natural Gas Company.

In return for the sale to Algonquin of the 114,835,686 MCF which are in issue in this case, Texas Eastern received the amount of $49,042,131. It is the allocation of these specific receipts to New Jersey for purposes of com-

puting the business allocation formula which Texas Eastern claims is unlawful. Most important, however, is the fact that these receipts were not allocated to any other state for purposes of computing that state's franchise tax. Algonquin, being an independent corporate entity selling and transporting natural gas for profit, resold the 114,835,686 MCF it purchased from Texas Eastern for the amount of $65,120,457.81, thus making a gross profit on this transaction of $16,078,326.81.

All of the sales and transfers of natural gas by Texas Eastern which occurred in New Jersey in 1967 to the three New Jersey utilities and to Algonquin constituted what are denominated in the Natural Gas Act as "sales for resale" (15 U.S.C. 717). In each such sale, the natural gas was physically transferred without interruption in movement from the pipelines of Texas Eastern to the connecting pipelines of either the New Jersey utilities or Algonquin. The only mechanical difference between the transfer of the natural gas on the one hand to Algonquin, and on the other hand to the New Jersey utilities, was that the pressure of the flow was reduced in the latter transfer in order to permit the distribution of the gas to the New Jersey facilities.

New Jersey is only remotely and incidentally connected with the interstate transaction. The natural gas flowed from wells in Texas and Louisiana into Texas Eastern's interstate pipeline system; transported through southern and midwestern States. It passed uninterrupted and at high pressure into Algonquin's interstate pipeline system and continued its interstate journey at high pressure in Algonquin's pipelines to its ultimate destinations out of New Jersey. The gas was thus carried from States outside New Jersey, through New Jersey in Texas Eastern's and Algonquin's interstate systems to distributors outside New Jersey

in unbroken movement in the stream of interstate commerce.

In reality, New Jersey is just one of the many States through which the gas passed in the flow of commerce, and, by geographical circumstance, merely happened to be the place where the gas moved without pause or interruption from one interstate pipeline to another. The transfer was an integral, inseparable part of the interstate process. Without it, there could be no interstate commerce.

During 1967, Texas Eastern had extensive facilities in New Jersey for the purpose of maintaining and operating its pipeline system. Its facilities consisted of 209.6 miles of underground pipeline, a maintenance office in Linden and various measuring and regulating equipment necessary and appurtenant to the operation of its pipeline system. The value of this property was in excess of $39 million. The measuring equipment, which was located at the points of transfer, automatically measured and recorded, by means of a calibrated orifice plate and other instrument's the volume of natural gas flowing from Texas Eastern's pipelines to those of its customers. The company employed 29 people in this State commanding a total payroll of $214,376.28.

The Corporation Business Tax is computed by adding together prescribed percentages of allocated net worth (stockholders book equity) plus allocated net income (related to taxable income as reported to the federal government, with certain exceptions not here pertinent). N.J.S.A. 54:10A-4(d) and (k) and 5. The Act recognized that many corporations doing business in New Jersey maintain business activities in other states as well.

In order to provide a fair method for allocation, the statute employs a formula which attempts to relate the taxpayer's New Jersey business to that exercised by the total

franchise. For the purpose of allocating to New Jersey the net worth of a company with multi-state activities, the statute prescribes two basic formulas. The tax is measured by the formula allocating the greater portion of net worth to this State. N.J.S.A. 54:10A-5(b) utilizes the ratio of the average value of assets (including intangible assets) in New Jersey to assets everywhere. This three-part formula, which is denominated as the "business allocation factor," produced a higher percentage than the "asset allocation factor" and therefore was the formula used in 1967 to allocate the taxpayer's net worth. The net income part of the tax in the case of a multi-state company is always ascertained by use of the business allocation factor, N.J.S.A. 54:10A-5(c) and 6.

Thus for the year 1967, the taxpayer utilized the business allocation factor to compute the amount of net worth and net income to be allocated to New Jersey. The business allocation factor is based on the average of the following three fractions.

"1. The value of the taxpayer's real and tangible personal property within the State over the value of all such property wherever situated.

2. The taxpayer's gross receipts from sales of tangible personal property, services performed, rentals from property and all the business receipts earned within the State over the total of such receipts whether within or without the State.

3. The total wages, salaries and other personal service compensation of officers and employees within the State over the total of such compensation within and without the State." *F.W. Woolworth Co. v. Director of Division of Taxation*, 45 N.J. 466, 475 (1965).

In the present case, Texas Eastern is contesting the validity of appropriating to New Jersey those receipts from Algonquin representing deliveries of natural gas to out-of-state sources for purposes of computing the receipts portion of the business allocation factor. It is important to note that the receipts in question were not actually "*taxed*" by New Jersey, but were utilized to compute the allocation formula. N.J.S.A. 54:10A-6(B) provides that the receipts' portion of the allocation factor is to be computed in the following way:

"The receipts of the taxpayer, computed on the cash or accrual basis according to the method of accounting used in the computation of its net income for Federal Tax purposes, arising for such period from

(1) sales of its tangible personal property located within this State at the time of the receipt of or appropriation to the orders where shipments are made to points within the State,

(2) sales of tangible personal property located without the State at the time of the receipt of or appropriation to the orders where shipment is made to points within the State,

(3) Deleted by amendment.

(4) services performed with the State,

(5) rentals from property situated, and royalties from the use of patents or copyrights, within the State,

(6) All other business receipts (excluding dividends excluded from entire net income by subsection (k)(1) of section 4 hereof) earned within the State, divided by the total amount of the taxpayers' receipts, similarly computed, arising during such period from all sales of its tangible personal property, services, rentals, royalties and all other business receipts, whether within or without the State;"

Subpart (2) of N.J.S.A. 54:10A-6(B) thus specifically includes in the numerator of the receipts fraction the receipts from sales of property located out of State" . . . where shipment is made to points within the State." The facts in this case indicate that Texas Eastern owned the natural gas it transported and physically transferred to Algonquin in New Jersey. The term shipment has been defined as "delivery," *Campbell River Mills Co. v. Chicago, M. St. P. & P. R. Co.*, 42 F.2d 775, 777 (W.D.N.D. 1930), aff'd 53 F.2d 69 (9th Cir. 1931), *cert.* den. 285 U.S. 530, 52 S.Ct. 310, 76 L.Ed. 930 (1932), and as "the act or process of having goods transported to a designated place." *Chicago R. I. & P. Ry. Co. v. Petroleum Refining Co.*, 39 F.2d 629, 631 (E.D. Kt. 1930). Texas Eastern relinquished possession of the natural gas at the point where its pipelines connected with those of Algonquin in New Jersey. Thus the physical transfer of the natural gas by Texas Eastern to the adjoining pipeline of Algonquin in New Jersey satisfies the requirement that "shipment" occurred within the State.

The transfer of the natural gas, because of its physical nature, is always accomplished by means of "uninterrupted movement." The transfer of the natural gas to the three New Jersey public utilities also involved uninterrupted movement in interstate commerce. The transfer to the three public utilities was therefore accomplished in the same manner as the transfer to Algonquin. Each of these transfers involved the receipt of funds on the part of Texas Eastern, which funds represented the earnings of the taxpayer.

A Corportion engaged in an interstate business is not exempt from State taxation if some "nexus" of local, intrastate activities links it to a particular taxing jurisdiction. See *General Motors Corp. v. State of Washington*, 377 U.S. 436 (1964). Yet, should the "nexus" be found, the tax must fairly relate to the value of in-state exercise of the corporate franchise and not be levied upon benefits derived from operations which are distinctly interstate in character.

Accordingly, in evaluating a tax, ". . . the question is whether the State has exerted its power in proper proportion to . . . (the taxpayer's) activities within the State and to . . . (the taxpayer's) consequent enjoyment of the opportunities and protections which the State has afforded. Where . . . the taxing State is not the domicilary State, we look to the taxpayer's business activities within the State; *i.e.*, the local incidents, to determine if the gross receipts from sales therein (or other basis of the tax) may be fairly related to those activities." *General Motors Corp. v. State of Washington, supra* (377 U.S. at 411); *General Motors Corporation v. District of Columbia*, 380 U.S. 553 (1965). Accordingly, apportionment formulas must, both in conception and mechanical operation, fairly reflect and relate the real extent and value of local corporate activities. *General Motors Corp. v. State of Washington, supra; General Motors Corporation v. District of Columbia, supra.*

Certain decisions of the New Jersey Supreme Court, involving the Corporation Business Tax Act, illustrate the frame of reference necessary to the evaluation. See *F. W. Woolworth Co. v. Director of Division of Taxation*, 45 N.J. 466 (1965); *Roadway Express, Inc. et al v. Director, Division of Taxation*, 50 N.J. 471 (1967).

It is illogical for petitioner to contend that the Legislature meant to exclude certain receipts from constituting New Jersey receipts merely because the ultimate destination of the property subsequent to the sale (from which the receipts in question were derived were out-of-state). The essential fact is that Texas Eastern was not the party

transporting the natural gas out-of-state. This latter transportation was accomplished by a different corporate entity, Algonquin, which has actual ownership rights of this gas at the time such out-of-state movement was in process. Texas Eastern's involvement in the transaction *ceased* in New Jersey when it relinquished its ownership rights over the gas. The receipts of this transaction were, therefore, New Jersey receipts for purposes of the allocation formula since the sale of the natural gas by Texas Eastern to Algonquin involved the shipment of gas to a point within the State where the transfer occurred.

The fact that Texas Eastern negotiated the contracts with Algonquin outside of the State did not destroy the nexus New Jersey had with these transfers and resulting receipts, since the nexus or connection requirement was satisfied by virtue that the actual transfers and sales took place in New Jersey. In *International Harvestor Co. v. Department of Treasury of State of Indiana,* 322 U.S. 340, 345, 64 S. Ct. 1019, 88 L. Ed. 1313 (1944), the court noted that:

> "The fact that the sales . . . are made by an out-of-state seller and that the contracts were made outside the State is not controlling. Here . . delivery of the goods in Indiana is an adequate taxable event."

The fact that the natural gas was destined to be transported out-of-state immediately after the transfer took place did not immunize the receipts from that transaction from either being directly taxed or being considered New Jersey receipts to compute the franchise tax allocation formula. The essential transaction in this case, namely the actual physical transfer of the gas, took place *only* in New Jersey.

The Supreme Court has in fact established in a long line of cases the propriety for states to utilize in-state

aspects of interstate commerce to compute state franchise tax allocation factors. In the case of *Underwood Typewriter Co v. Chamberlain,* 254 US. 113, 41 S. Ct. 45, 65 L. Ed. 165 (1920), the Court upheld the validity of a Connecticut franchise tax which attempted to compute, by means of an allocation formula, the amount of the taxpayer's total income derived from interstate commerce which was related to Connecticut. The Court thus stated that:

> "A tax is not obnoxious to the commerce clause merely because it is imposed upon property used in interstate commerce, even if it takes the form of a tax for the privilege of exercising its franchise within the state. (citations omitted). This tax is based upon the net profits earned within that state. That a tax measured by new profits is valid, although these profits may have been derived in part, or indeed mainly, from interstate commerce, is settled." 254 U.S. at 120.

Similarly in the present case, the receipts derived by Texas Eastern from Algonquin are a means of measuring profits earned in this State. The fact that the receipts have been derived from an interstate transaction does not immunize such receipts from being used to compute the allocation formula. In *International Harvester Co. v. Evatt,* 329 U.S. 416, 67 S. Ct. 444, 91 L. Ed. 390 (1947), the Supreme Court specifically upheld the right of a state to utilize the receipts from an interstate sale for purposes of computing a state franchise allocation formula.

The court rejected the taxpayer's arguments that the utilization of receipts from interstate commerce in the numerator of the apportionment formula was violative of both the due process and the commerce clauses:

> "Nor does the fact that a computation such as that under Ohio's law includes receipts from interstate sales

affect the validity of a fair apportionment (citation omitted)." 329 U.S. at 421.

The court further noted that,

"A state's tax law is not to be nullified merely because the result is achieved through a formula which includes consideration of interstate and out-of-state transactions in their relation to the intrastate privilege." 329 U.S. at 423.

The utilization by New Jersey of Texas Eastern's receipts from Algonquin in the numerator of the sales fraction of the business allocation factor is clearly proper in view of the *Evatt* decision. In *Hump Hairpin Manuf. Co. v. Emmerson*, 258 U.S. 290, 42 S. Ct. 305, 66 L. Ed 622, (1922), the court again sustained an Illinois franchise tax which included interstate sales as part of Illinois business for the purpose of an allocation formula. A state, thus, may properly establish a formula based on in-state aspects of interstate commerce for determining that portion of net income or net worth properly attributable to business within the state, including that from interstate commerce. *Maxwell v. Kent-Coffey Mfg. Co.*, 204 N.C. 365, 168 S.E. 397, 90 A.L.R. 476 (Sup. Ct. 1933), aff'd 291 U.S. 642, 54 S. Ct. 437 78 L. Ed. 1040 (1933). See also *Western Cartridge Co. v. Emmerson*, 281 U.S. 511, 50 S. Ct. 383, 74 L. Ed. 1004 (1930); *West Publishing Co. v. McColgan*, 27 Cal. 2d 705, 166 P. 2d 861 (Sup. Ct. 1946), aff'd 328 U.S. 823, 66 S. Ct. 1378, 90 L. Ed. 1603 (1945); *State Tax Commission v. John H. Breck, Inc.*, 336 Mass. 277, 144 N.E. 2d 87 (Sup. Jud. Ct. 1957); *United States Steel Corp. v. Undercofler*, 220 Ga. 553, 140 S.E. 2d 269 (Sup. Ct. 1965).

The courts, moreover, have recognized the necessity for states to utilize in-state aspects of interstate commerce in order to properly allocate to the taxing state the business of a multi-state company. In *Butler Bros. v. McColgan*,

315 U.S. 501, 62 S. Ct. 701, 86 L. Ed. 991 (1942), the court upheld the validity of a California franchise tax which used the same three-part allocation formula as in the New Jersey Tax to compute the tax liability of a multi-state corporation. Despite the fact that the taxpayer corporation actually sustained a loss in California under a separate accounting method, the court, nevertheless, upheld the application of the allocation formula:

"We cannot say that property, payroll and sales are inappropriate ingredients of an apportionment formula. We agree with the Supreme Court of California that these factors may properly be deemed to reflect the relative contribution of the activities in the various states to the production of the total unitary income, so as to allocate to California its just proportion of the profits earned by appellant from this unitary business." 315 U.S. at 509.

The same result was reached by the court in *Bass, Ratcliff & Gretton, Ltd. v. State Tax Commission*, 266 U.S. 271 45 S. Ct. 82, 69 L. Ed. 282 (1924).

Petitioner disputes this body of case law and cites three cases to support its contention that receipts from interstate sales cannot be employed in determining New Jersey business for allocation purposes. (*Michigan-Wisconsin Pipe Line Co. v. Calvert*, 347 U.S. 157, 74 S. Ct. 396, 98 L. Ed. 583 (1954); *Dunbar-Stanley Studios, Inc. v. Alabama*, 393 U.S. 537, 89 S. Ct. 757, 21 L. Ed. 2d 759 (1969); *Panhandle Eastern Pipe Line Company v. Michigan Corporation and Securities Commission*, 246 Mich. 50, 77 N.W. 2d 249 (Sup. Ct. 1956).)

A brief discussion of each of these cases will indicate their inapplicability to the case at hand. In the case of *Panhandle Eastern Pipe Line Company v. Michigan Corporation and Securities Commission, supra*, which involved

the same issue begin litigated in the present case, the court held that using receipts from an interstate sale could not be considered Michigan business for purposes of the Michigan franchise tax allocation factor. The Michigan Supreme Court, however, in two subsequent decisions involving the same basic issue, has severely criticized the *Panhandle* decision and reversed its position. In *Duluth South S. A. D. Co. v. Michigan Corp. & Sec. Com'n*, 353 Mich. 636, 92 N.W. 22, 37-38 (Sup. Ct. 1958), *cert.* den. 359 U.S. 310, 79 S. Ct. 876, 3 L. Ed. 831 (1958), the court made the following statement:

> ". . .Panhandle . . . relied upon Cooney v. Mountain States Telephone & Telegraph Co., supra, for constitutional authority. (It) failed to distinguish between the direct taxation of *interstate commerce* (which Cooney ruled out) and the employment of an interstate-commerce factor in the formula for determining the amount of paid-up capital and surplus to be allocated to Michigan in computing the fee to be assessed for doing *intrastate* business in Michigan.
>
> *We find no United States Supreme Court precedent which interprets the commerce clause as forbidding use of such an allocation formula unless the result is shown to be unreasonable or discriminatory.*
>
> We now limit the application of the opinions in Gartland and Panhandle and hold that there is no constitutional barrier to the use of an interstate-commerce factor in the allocation formula for determining the portion of paid-up capital and surplus allocation to Michigan for computation of a franchise tax for the right to carry on intrastate business in Michigan where, as here, there is no showing that such formula reaches an unreasonable or discriminatory results." (emphasis added).

In *Wisconsin & Michigan Steamship Company v. Corporation and Securities Commission*, 371 Mich. 61, 123 N.W. 2d 258, 262 Sup. Ct. (1963), *cert.* den. 376 U.S. 912, 84 S. Ct. 668, 11 L. Ed. 2d 610 (1964), the Michigan Supreme Court noted that it has "severely limited" the *Panhandle* decision in the *Duluth* case and "realistically considered, overruled" the *Panhandle* holding that interstate business must be excluded from consideration in determining the apportionment formula used in computing the franchise fee. The *Panhandle* case, therefore, has no legal precedential value and is not applicable to the present matter.

Petitioner also heavily relies on the holding in *Michigan-Wisconsin Pipe Line Co. v. Calvert, supra*, which involved a Texas franchise tax imposed upon a natural gas pipeline company for the "taking" or "exit of the gas from the State." 347 U.S. at 167. The Court held this tax burdensome on interstate commerce because it was a tax on the privilege of engaging in interstate commerce and specifically noted that the incidence of the tax was not on the passing of title since the "levy was designed to avoid taxing the sale." 347 U.S. at 169. The Court thus clearly implied that a tax on the actual sale of the natural gas would have been proper since such a tax would not be for the privilege of engaging in interstate commerce. By the same token, the utilization of the receipts in question as a measure of the amount of New Jersey business conducted by Texas Eastern does not constitute a levy for the privilege of conducting interstate commerce. *Michigan-Wisconsin*, therefore, is not germane to the issue at hand.

The *Dunbar* decision involved strictly a subjectivity question, namely whether an Alabama tax placed on traveling photographers who were employed by a North Carolina company but performed some of their services within the state of Alabama, was constitutionally proper. The

Court, in upholding the tax, noted that a privilege tax on an interstate enterprise would not be upheld where that enterprise has only the minimal contracts with the taxing state of soliciting orders through traveling salesmen and delivering merchandise.

The issue in the present case involves solely the right of New Jersey to utilize the receipts in question in the numerator of the sales allocation factor for purposes of computing the petitioner's allocated net income and net worth tax bases. The *Dunbar* decision has no application to that issue since it was concerned with the issue of subjectivity to a state franchise tax, which is a matter not in dispute in the present case.

The taxpayer has the burden of showing that the apportionment in question actually imposes a multiple burden on its activities. Petitioner attempts to meet this burden by indicating that Algonquin paid franchise taxes in other states in which the natural gas, which it purchased from Texas Eastern in New Jersey, was delivered. Again it must be stated that New Jersey did not tax these receipts (even though, as indicated, it constitutionally would have a legitimate right to tax these receipts under a sales tax or gross receipts tax) but merely utilized these receipts to formulate a franchise tax allocation formula in order to avoid imposing a multiple burden upon petitioner's franchise. The fact that no other state utilized these receipts to compute its franchise tax allocation factor assured Texas Eastern of not being subjectetd to a multiple burden.

Algonquin, of course, is a separate corporate entity which transports and sells natural gas for profit. The very same natural gas transferred by Texas Eastern to Algonquin in 1967 was in turn resold by Algonquin for a profit of $16,078,326.81. Algonquin was thus properly assessed franchise taxes in those states where it carried on the business

which was the source for its corporate profits. The imposition of foreign franchise taxes upon Algonquin was not a burden upon Texas Eastern. Manufacturing, wholeselling, jobbing and retailing concerns must all pay their fair share of franchise taxes regardless of the fact that they may deal with the same products at different stages of time. In order to demonstrate that the New Jersey formula burdened interstate commerce, the petitioner must show that another state was utilizing the receipts in question to place an additional franchise tax burden upon Texas Eastern's activities. *General Motors Corp. v. Washington, supra.* Petitioner has failed to show such a burden. The fact that another corporate entity, Algonquin, was paying taxes to foreign state is of no consequence to Texas Eastern.

The Corporation Business Tax Act provides that the Director may adjust the business allocation factor, with respect to its application to either net worth or net income or both if it appears to him that the factor determined pursuant to N.J.S.A. 54:10A-6,

> "does not properly reflect the activity, business, receipts, capital, entire net worth or entire net income of a taxpayer reasonably attributable to the State . . . by
>
> (a)excluding 1 or more of the factors therein;
>
> (b)including 1 or more other factors, such as expenses, purchases, contract values (minus subcontract values);
>
> (c) excluding 1 or more assets in computing entire net worth; or
>
> (d) excluding 1 or more assets in computing an allocation percentage; or
>
> (e) applying any other similar or different method calculated to effect a fair and proper allocation of the

entire net income and the entire net worth reasonably attributable to the State." *See F. W. Woolworth Co. v. Director of Div. of Tax., supra,* 45 N.J. at 475-476.

In order for the Director to exercise his discretion and make adjustments to a taxpayer's business allocation factor, there must be a showing that the statutory allocation factor works an "unfairness" upon the taxpayer. *F. W. Woolworth Co. v. Director of Div. of Tax., supra* at 947. The petitioner has failed to indicate the specific unfairness of the statutory formula. The receipts in question are allocated only to this State. If New Jersey did not allocate these receipts, then, in fact, the receipts from Algonquin would not be utilized by any state to formulate an apportionment formula. Certainly such a result would be unfair to the other multi-state corporations whose in-state receipts are allocated to New Jersey.

The March 5, 1973 decision of the United States Supreme Court in *United Air Lines, Inc. v. Mahin* (41 Law Week 4378) appears to set forth the guide lines for the determination of this case. Under that decision if Texas Eastern gas flowed through the State of New Jersey without any measurement or transfer of ownership, Texas Eastern would not be subject to being taxed in this jurisdiction under doctrine of the case of *Michigan-Wisconsin Pipeline Co. v. Calvert,* 347 U.S. 157 (1954).

However, where the fuel is stored in the State for periods ranging from two to twelve days and then continues to be used for interstate consumption, the storage or the withdrawal from storage constitutes a taxable event and does not impose an unconstitutional burden on interstate commerce. Here the measurement and transfer of ownership constitutes the taxable event, which is also in accordance with the cases of *Edelman v. Boeing Air Transport, Inc.*

289 U.S. 249 (1933) and *Nashville, Chattanooga & St. Louis R. Co. v. Wallace,* 288 U.S. 249 (1933).

I direct the entry of judgment affirming the directors determination of the tax liability in this matter. Rit By Hand.

DATED: May 22nd, 1975.

/s/ Joel A. Mott
J.D.T.A.

JUDGMENT
(Filed July 10, 1975)

This matter having come before the Division of Tax Appeals on the petition of Texas Eastern Transmission Corporation, and the matter having been tried before the Honorable Joel A. Mott, J.D.T.A., on a stipulation of facts, and Jeffers and Dillon, Esqs., appearing for the petitioner, Texas Eastern Transmission Corporation, and George F. Kugler, Attorney General of New Jersey, by Harry Haushalter, Deputy Attorney General, appearing for the respondent, Director of the Division of Taxation, and the Division of Tax Appeals having reviewed the record and the respective briefs of the parties, and Judge Joel A. Mott having rendered an opinion dated May 22, 1975, which was approved by the Division of Tax Appeals on June 5, 1975, and further good cause appearing;

IT IS on this 10th day of July , 1975

ORDERED AND ADJUDGED as follows:

1. That the Director of the Division of Taxation's denial of the petitioner's claim for adjustment under the New Jersey Corporation Business Tax Act, N.J.S.A. 54:10A-1 *et seq.*, for the petitioner's 1967 tax year be affirmed.

2. That the numerator of the receipts portion of the business allocation factor as noted in the petitioner's 1967 corporation business tax return as filed should properly include and reflect as New Jersey receipts the $49,042,131.00 of receipts received by the petitioner from Algonquin Gas Transmission Company representing payment for natural gas transferred by the petitioner to Algonquin Gas Transmission Company in this State.

3. That the petitioner's tax liability under the New Jersey Corporation Business Tax Act for its 1967 tax year is $174,173.58.

/s/ Joel A. Mott
JOEL A. MOTT, J.D.T.A.

Attest:

/s/ Barbara McConnell
BARBARA McCONNELL
Administrative Secretary
Division of Tax Appeals

I hereby consent to the form of the within Judgment.

JEFFERS AND DILLON, ESQS.
Attorneys for Petitioner

By: /s/ Thomas J. Bitar
THOMAS J. BITAR

ORDER DENYING DIRECT CERTIFICATION

This matter having been duly presented to the Court, it is ORDERED that the motion for direct certification is denied.

WITNESS, the Honorable Richard J. Hughes, Chief Justice, at Trenton, this 11th day of March, 1976.

DATED: March 11, 1976.

A TRUE COPY

/s/ Stephen W. Townsend,
Acting Clerk

/s/ Florence R. Peskoe,
Clerk

OPINION OF THE APPELLATE DIVISION

Argued: June 15, 1976—Decided: June 23, 1976.

Before Judges Lynch, Larner and Horn.

On appeal from the Division of Tax Appeals.

Mr. Thomas J. Bitar argued the cause for appellant (Messrs. Dillon and Bitar, attorneys; Messrs. Bitar and William F. Campbell, III, on the briefs).

Mr. Harry Haushalter, Deputy Attorney General, argued the cause for respondent (Mr. William F. Hyland, Attorney General, attorney; Mr. Stephen Skillman, Assistant Attorney General, of counsel).

PER CURIAM

The judgment of the Division of Tax Appeals is affirmed substantially for the reasons stated in the opinion of Judge Mott, dated June 5, 1975.

A TRUE COPY

/s/ Elizabeth McLaughlin,
Clerk

DENIAL OF PETITION FOR CERTIFICATION
(Filed October 25, 1976)

To Appellate Division, Superior Court:

A petition for certification having been submitted to this Court, and the Court having considered the same,

It is hereupon ORDERED that the petition for certification is denied with costs.

WITNESS, the Honorable Richard J. Hughes, Chief Justice, at Trenton, this 25th day of October, 1976.

A TRUE COPY

/s/ Florence R. Peskoe,
Clerk

ORDER DISMISSING APPEAL
(Filed October 25, 1976)

This matter having been duly presented to the Court, it is ORDERED that the appeal is dismissed pursuant to Rule 2:12-9.

WITNESS, the Honorable Richard J. Hughes, Chief Justice, at Trenton, this 25th day of October, 1976.

A TRUE COPY

/s/ Florence R. Peskoe,
Clerk

NOTICE OF APPEAL TO THE SUPREME COURT OF THE UNITED STATES

(Filed January 5, 1977)

Notice is hereby given that Texas Eastern Transmission Corporation, the appellant above named, hereby appeals to the Supreme Court of the United States from a final judgment of the Supreme Court of the State of New Jersey dismissing its appeal entered in this action on October 25, 1976.

This apeal is taken pursuant to 28 U.S.C. §1257(2).

DILLON and BITAR
Attorneys for Texas Eastern
Transmission Corporation,
Appellant

By: /s/ Sidney G. Dillon
A Member of the Firm
53 Maple Avenue,
Morristown, New Jersey 07960
(201) 539-3100

AFFIDAVIT OF SERVICE

I, WILLIAM F. CAMPBELL, III, being of full age and duly sworn according to law, upon my oath depose and say:

1. I am an attorney employed by the law firm of Dillon and Bitar, attorneys for Texas Eastern Tranmission Corporation, the appellant in the above entitled action.

2. On January 3, 1977, I placed in the mails at the U.S. Post Office in Morristown, New Jersey, a sealed envelope with postage prepaid thereon, by certified mail, return receipt requested, addressed to

William F. Hyland, Attorney General
Attn: Harry Haushalter, Deputy Attorney General
at said addressee's post office address at
State House Annex
Trenton, New Jersey 08625

containing one copy of the Notice of Appeal in the above encaptioned action.

3. All parties required to be served in this action have been served.

4. The foregoing statements made by me are true, I am aware that if any of the foregoing statements made by me are willfully false, I am subject to punishment.

/s/ William F. Campbell, III
WILLIAM F. CAMPBELL, III

NOTARIZED

DILLON AND BITAR
Attorneys for Texas Eastern
Transmission Corporation,
Appellant
53 Maple Avenue,
Morristown, N.J. 07960
(201) 539-3100

STATUTORY MATERIALS

N.J. STAT. ANN. §54:10A-6

In the case of a taxpayer which maintains a regular place of business outside this State other than a statutory office, the portion of its entire net worth to be used as a measure of the tax imposed by section 5(a) of this act, and the portion of its entire net income to be used as a measure of the tax imposed by section 5(c) of this act, shall be determined by multiplying such entire net worth and entire net income, respectively, by an allocation factor which shall be the average of the fractions computed in (A), (B) and (C) below, or of so many of them as may be applicable, that is:

(A) The average value of the taxpayer's real and tangible personal property within the State during the period covered by its report divided by the average value of all the taxpayer's real and tangible personal property wherever situated during such period:

(B) The receipts of the taxpayer, computed on the cash or accrual basis according to the method of accounting used in the computation of its net income for Federal tax purposes, arising during such period from

(1) sales of its tangible personal property located within this State at the time of the receipt of or appropriation to the orders where shipments are made to points within this State,

(2) sales of tangible personal property located without the State at the time of the receipt of or appropriation to the orders where shipment is made to points within this State,

(3) Deleted by amendment.

(4) services performed within the State,

(5) rentals from property situated, and royalties from the use of patents or copyrights, within the State,

(6) All other business receipts (excluding dividends excluded from entire net income by subsection (k) (1) of section 4 hereof) earned within the State, divided by the total amount of the taxpayer's receipts, similarly computed, arising during such period from all sales of its tangible personal property, services, rentals, royalties and all other business receipts, whether within or without the State;

(C) The total wages, salaries and other personal service compensation, similarly computed, during such period of officers and employees within the State divided by the total wages, salaries and other personal service compensation, similarly computed, during such period of all the taxpayer's officers and employees within and without the State.

In the case of a taxpayer which does not maintain a regular place of business outside this State other than a statutory office, the allocation factor shall be 100%.

N.J. STAT. ANN. §54:10A-8

If it shall appear to the commissioner that an allocation factor determined pursuant to section 6 [1] does not properly reflect the activity, business, receipts, capital, entire net worth or entire net income of a taxpayer reasonably attributable to the State, he may adjust it by:

(a) excluding one or more of the factors therein;

(b) including one or more other factors, such as expenses, purchases, contract values (minus subcontract values);

(c) excluding one or more assets in computing entire net worth; or

(d) excluding one or more assets in computing an allocation percentage; or

(e) applying any other similar or different method calculated to effect a fair and proper allocation of the entire net income and the entire net worth reasonably attributable to the State.